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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)	
	)	
Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992	)	MM Dkt. No. 92-266
	)	
	)	
Rate Regulation	)	

REPLY COMMENTS OF COMCAST CABLE COMMUNICATIONS, INC. ON THE FURTHER NOTICE OF PROPOSED RULEMAKING

Comcast Cable Communications, Inc. ("Comcast"), by its attorneys, hereby submits its reply comments in the above-referenced proceeding.[1/] The Further Notice proposed to exclude systems that have 30 percent or lower penetration from the statutory definition of "effective competition" for the purpose of determining cable rate benchmarks. For the reasons described below and in the affidavit of George R. Schink (the "Schink Affidavit"), attached hereto as Exhibit A, Comcast submits that the Commission should reject the proposal in the Further Notice and retain the statutory definition of effective competition for the purpose of determining permissible rates.

The commenters urging the Commission to exclude from its study cable systems that are subject to effective competition and that have 30 percent or lower penetration failed to provide any valid legal rationale which would sustain

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1/ Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992, Report and Order and Further Notice of Proposed Rulemaking, MM Dkt. No. 92-266, FCC 93-177 (released May 3, 1993) (the "Further Notice").

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their position. As Comcast demonstrated in its comments,[2/] the Commission has no discretion to choose when to use the statutory definition of "effective competition." Section 623(*l*) of the Communications Act states clearly that the 3-prong definition of effective competition applies to all of Section 623, including the subsections that define the criteria for determining permissible rates. 47 U.S.C. § 533(*l*). When the statute is clear, the Commission must follow the mandate of the statutory language. See American Civil Liberties Union v. F.C.C., 823 F.2d 1554, 1557 (D.C. Cir. 1987) (the Commission cannot adopt a definition that differs from the one in the statute).

The Commission should reject claims of certain commenters that low-penetration systems should be excluded from benchmark determinations. The analyses that purport to show that low-penetration systems have the "wrong" characteristics to be used in benchmark determinations are of no probative value.[3/] As shown in the Schink Affidavit, these studies have both analytic and methodological flaws. Both analyses, for instance, assume that the "correct" rate must be lower than the rates found by the Commission. There is, however, no basis for this assumption except the desire of the Telephone Companies and CFA to have the Commission set lower benchmarks. Schink Affidavit at 4-5. In addition, both the Telephone Companies and CFA, in excluding the low-penetration data, would leave the Commission with a sample so small that it

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2/ Comments of the Joint Parties, filed June 17, 1993.

3/ These analyses were attached to the Comments of Bell Atlantic, GTE and the NYNEX Telephone Companies (the "Telephone Companies") and the Comments of the Consumer Federation of America ("CFA").

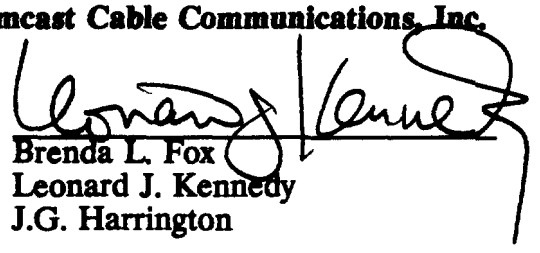
could not be used to reliably predict anything about the 33,000 community units the 1992 Cable Act governs. Id. at 7-8.

There are many other flaws in these analyses, ranging from the

For all of these reasons, Comcast urges the Commission to reject the proposal in the Further Notice and continue to define "effective competition" as the statute requires.

Respectfully submitted,

Comcast Cable Communications, Inc.

By: 
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Its Attorneys

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July 2, 1993

EXHIBIT A

Affidavit of George R. Schink

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)	
	)	
Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992 Rates Regulation	)	MM Docket 92-266

AFFIDAVIT OF GEORGE R. SCHINK

George R. Schink deposes and says:

1. I am Chairman and CEO of the AUS Consultants, Industry Analysis Group. My business address is AUS Consultants, Industry Analysis Group, 200 Four Falls Corporate Center, Suite 308, West Conshohocken, Pennsylvania 19428. My experience involves a broad range of economic analyses of market structure and dynamics in several industries. In addition, I have presented testimony in numerous proceedings before state and Federal regulatory agencies, in state and Federal courts, and before Congress.

2. I was awarded a B.S. in Economics from the University of Wisconsin at Madison in 1964, and a Ph.D. in Economics at the University of Pennsylvania in 1971. I was a lecturer in the Department of Economics at the University of Maryland from 1968 through 1972, where I taught various courses in economics, mathematics and econometrics. I also served as a visiting lecturer on economics at the University of Pennsylvania in 1973. I was also

Research Fellow of the University of Pennsylvania's Economic Research Unit on behalf of Lawrence R. Klein (1965-1968), and the Resident Principal Investigator for the Quarterly Model Project of the Brookings Institution (1969-1972).

From 1972 through 1988, I held a number of positions with The WEFA Group (formerly Wharton Econometric Forecasting Associates) in Bala Cynwyd, Pennsylvania, including Executive Director of Special Projects, Executive Director of the Wharton Annual Model Project, Vice President of the U.S. Modeling Services, Senior Vice President of Consulting Services, and Vice President of Research and Development. I assumed my current position as Chairman and Chief Executive Officer of AUS Consultants, Industry Analysis Group in June of 1988.

I have included in my resume, which is attached as an Appendix, a list of my appearances as an expert witness together with a list of my pertinent research publications.

A. Introduction and Overview

3. In its initial order[1], the Commission computed benchmark rates for cable systems based on its estimate of the prices charged per channel by cable systems that the 1992 Cable Act defined to be

[1]Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992, Rate Regulation, Report and Order and Further Notice of Proposed Rulemaking, FCC 93-177 (released May 3, 1993) at Appendix E and ¶207 (hereinafter Initial Order).

subject to effective competition[2]. The 1992 Cable Act defined systems subject to effective competition to include:

a) Systems where less than 30 percent of the households in the franchise area subscribe to the system (i.e., low penetration or Type A systems).

b) Systems whose franchise area is served by at least two unaffiliated systems with offers service to at least 50 percent of the households in the franchise area and in which at least 15% of the franchise area households subscribe to a system other than the largest system

Cooper and Gene Kimmelman).[4] The Bell Atlantic et al Comments and the CFA Comments advocate not utilizing the prices charged per channel by the low penetration systems (Type A) to calculate the benchmark rates. The CFA Comments go further and recommended that only the private overbuild subgroup (Type B) be used to calculate the benchmark rates.

B. Critique of the Bell Atlantic et al and CFA Comments

5. The Bell Atlantic et al Comments and the accompanying Hazlett Affidavit argue that the low penetration (Type A) systems rates should be excluded from the benchmark rate calculations because the Type A system average rates are no less than the average rates charged by systems deemed not to be subject to effective competitive (i.e., all other systems).[5] This fact may indicate that the average of all rates charged by all other systems is not above competitive system levels. If this is the case, then only those systems that have rates above the average rate may be charging rates that are "too high". One must keep in mind that the benchmark rate is intended to be a ceiling rate. If all other systems were constrained, in the absence of cost based justification for higher rates, to charge no more than the current average rate for all other systems (i.e. the benchmark rate was set

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[4]Comments of Consumer Federation of America, June 17, 1993 (hereinafter CFA Comments) and the attached data analysis (hereinafter CFA Data Analysis), MM Docket 92-266.

[5]Bell Atlantic et al Comments, pp. 5-6; Hazlett Affidavit, pp. 5-7.

equal to the average rate charged by all other systems), 50 percent of these systems would have to reduce their rates (i.e. approximately 15,000 of the 30,000 cable community units would reduce their rates). A price ceiling equal to the average rate for all other systems would still require substantial rate reductions.[6] The fact that Bell Atlantic et al and CFA have an a-priori belief that the price ceiling must be below the average rate charged by all other systems is no justification for excluding the Type A systems. The desired result should not be the basis for defining the method of calculation.

6. The Bell Atlantic et al Comments recommend reliance on the Type B and C systems to calculate benchmark rates. The Bell Atlantic et al Comments (and the Hazlett Affidavit) argue that there are reasons other than competition for the low penetration of the Type A systems. Dr. Hazlett enumerates several potential explanations for this low penetration including the fact that the rates charged by these systems are higher than those charged by the

all the other systems also low?

Dr. Hazlett also enumerates a number of demographic factors that he asserts could be the cause of low penetration rates by the Type A systems including household income, population ages, and seasonal use homes in an area (e.g., summer vacation homes). Finally, he adds poor cable service to the list of potential explanations.[8]

Dr. Hazlett purports to demonstrate that these factors explain low penetration by means of a casual survey of franchise area officials. Dr. Hazlett reports the remarks of several of these local community officials when they support his a-priori view that these factors other than competition have caused low penetration. The view points of single individuals in some of these communities does not provide any kind of scientific evidence supporting Dr. Hazlett's hypothesis. We don't have a complete list of all interviewees, we don't know what questions were asked, we don't have a record of the answers and the interviewees do not constitute a random sample of households that could be served by these low penetration systems. Mr. Hazlett's so-called "systematic survey" is simply the recording of anecdotal observations by a non-random sample of community officials in some of the communities served by the Type A systems. As such, it should be given no weight.

Given that Dr. Hazlett's survey provides no scientific support for his assertion that rates and franchise area demographic

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[8]Hazlett Affidavit, pp. 7-11.

characteristics cause low penetration, one is left with only his assertion that these factors, and not competition, explain low penetration. Merely showing, for example, that many of the low penetration franchise areas have low household income does not imply that low household income causes low penetration. It may be that the competitive alternatives to the cable system are more attractive to low income households. Dr. Hazlett would have to demonstrate that all cable systems had relatively low penetration rates in low income communities if he wanted to document that low income, and not competition, caused low penetration. Dr. Hazlett has provided no such documentation for the alleged effects of low income or for the alleged effects of any of the other franchise area demographic characteristics.

Finally, the benchmark rate is being computed to apply to the population of approximately 30,000 franchise areas (cable community units). Even including the Type A systems, the sample of competitive communities is 110 which is only 0.37 percent of the total population. Eliminating the Type A systems reduces the number to 46 which is only 0.15 percent of the population.

Generally, if one wants to estimate a population characteristic with accuracy, the sample size must be reasonably large. Without knowing exactly the probability distribution of the population being sampled, one cannot be very precise regarding the sample size needed to generate sufficient accuracy for a sample based estimate of a population characteristic. As a general rule, one can expect that a population characteristic (mean) will be

within plus or minus 5 percent of the sample based estimate with at least 95% confidence if the sample size is 384.[9] To be 95 percent confident that the population characteristic (mean) estimate is within plus or minus 10 percent of the sample based estimate, a sample size of 96 is required.[10] Clearly, sample sizes substantially below 100 do not provide reasonable sample based estimates of population characteristics.

7. The CFA Comments advocate relying solely in the rates charged by the Type B (private overbuild) systems to calculate the benchmark rates. They assert that the Type B systems are the only systems that have "characteristics similar to truly competitive market systems".[11] CFA does not attempt to refute the position that the Type A systems have low penetration due to competition. CFA merely observes that the low penetration systems have different average rates than the Type B systems and that they expect the causes leading to these differences to persist.[12]

No one is arguing that the Type B systems do not face intense competition and that, most likely, this intense competition has caused the rates charged by the Type B systems to be low. In fact, the competition could be so intense that the prices charged by

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[9]This sample size is based on estimating the sample proportion for a drawing from a binomial distribution where the "true probability" of success (or failure) is 0.5.

[10]Again, a binomial distribution is assumed with a true probability of success (or failure) of 0.5.

[11]CFA Comments, p.4.

[12]CFA Data Analysis, pp. 6-10.

these Type B systems have been driven down to the point where the revenues generated barely cover variable costs. A business will continue to operate so long as the revenues generated by its operations cover variable costs and any part of fixed costs (i.e., losses are smaller when the business operates then they would be if operations ceased). However, such a situation is not stable. No new investments will be made and, eventually the business will shut down because it can't justify replacing worn out equipment. A stable competitive environment requires that the firms in the industry are generating revenues sufficient to cover variable and fixed costs including a reasonable return on capital invested.

If one assumes that the rates charged by the Type B systems are sufficient to generate revenues just in excess of variable costs, then these rates are properly viewed as price floors and not price ceilings. If the prices charged do not generate revenues sufficient to cover variable costs, then the prices are not compensatory and the service provided in the franchise area is being cross subsidized by revenues generated elsewhere in the company.

An appropriate price ceiling is a price sufficient to earn a reasonable (competitive) return from a stand-alone replacement system for the franchise area (i.e., the cost, including a reasonable return or investment, to build a system to provide the

service just to the one franchise area).[13]

Finally, if the benchmark rate is calculated based solely on the sample of Type B systems, this rate, which will be applied to approximately 30,000 systems, will be computed based on a sample of 31 companies which is only 0.1 percent of the population. This is too small a sample to generate acceptably accurate estimates of the benchmark rates.

C. Other Issues

8. Neither the Bell Atlantic et al Comments nor the CFA Comments addressed a key issue in determining appropriate benchmark rates; namely, are the benchmark rates (prices) high enough to cover both variable and fixed costs including a reasonable (competitive) return on investment. The 1992 Cable Act indicates the FCC "may adopt formulas"[14] to determine basic rates for the cable community units (franchises). However, the 1992 Cable Act also indicates that these rates should allow the cable community units to earn "a reasonable profit".[15] The FCC has not tested whether the cable community units in its "competitive" group are earning a reasonable profit. If these units are not, on average, earning a reasonable profit, then their average rates are not a

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[13]As a practical matter, one might want to consider pricing at a system level. However, the FCC's analysis was performed at the franchise area level which is generally smaller, but could be bigger, than a system.

[14]1992 Cable Act, p. 1466 (B).

[15]1992 Cable Act, p. 1466 (C) (vii).

those effects have an effect on prices at the system level.

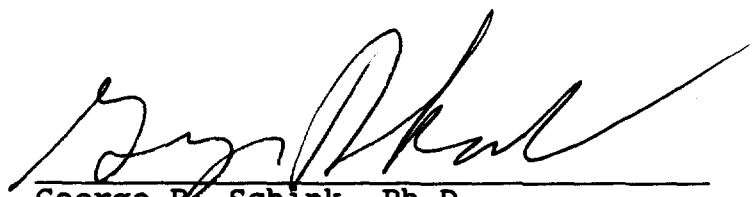
I have checked the FCC data file of 377 companies that was used by the FCC to perform its analysis. Some of the calculations do not appear to have been performed properly (e.g., the calculated price per channel is not always accurate). Until the entire file is checked, one cannot determine the effects of those problems. Nonetheless, it is not appropriate to finalize any conclusions until all the database calculations can be checked and corrected as required.

To the extent that the model used by the FCC tries to explain prices set at the system level using characteristics at the franchise level, one cannot be confident that these characteristics do not have a systematic effect on costs and prices. The FCC's view that some of these characteristics have no statistically significant effect on costs and prices may be due to commingling system and franchise area data.

D. Conclusions

10. The Commission has not been provided with any reliable indication that the low penetration systems are not competitive. The competitive sample is barely large enough to provide reasonably accurate estimates of the benchmark rates even when these low penetration systems are included. Excluding these systems would render the sample based estimates unreliable. As a result, the Commission should continue to include the low penetration systems in its calculation of the benchmark rates.

I declare under penalty of perjury under the laws of the United States of America that the foregoing is true and correct. Executed on the 2nd day of July, 1993.



George R. Schink, Ph.D.
Chairman & Chief Executive Officer
AUS Consultants
West Conshohocken, PA 19428

APPENDIX

RESUME OF GEORGE R. SCHINK

GEORGE R. SCHINK, Ph.D.
Chairman, Chief Executive Officer
AUS Consultants
Industry Analysis Group
200 Four Falls Corporate Center - Suite 308
West Conshohocken, PA 19428

PROFESSIONAL EXPERIENCE

AUS CONSULTANTS, INDUSTRY ANALYSIS GROUP, West Conshohocken, PA

Chairman and Chief Executive Officer — 6/88-Present

Responsible for overall management and strategic guidance of the Industry Analysis Group, as well as the design and execution of consulting projects related to the automotive, energy, utility, and telecommunications industries. These projects include market analysis, development of sales volume and revenue models, development of price and cost models, industry studies, and analysis of the impact of government policy and regulatory changes on these industries. The results of these studies are provided to clients as reports and in direct presentations to senior management. Also, Dr. Schink has extensive experience in presenting testimony before regulatory bodies and in the courts.

THE WEFA GROUP (Wharton Econometrics), Bala Cynwyd, PA

Senior Vice President, Consulting Services — 5/87-5/88
Vice President, Research and Development — 6/83-5/87

Responsible for the development, enhancement, specification, maintenance of the Wharton econometric models. Also responsible for design, execution, and economic content of large contract research projects, preparation and presentation of testimony, general quality control of Wharton economic analysis and forecasting products, internal training of economic staff, and design inputs for econometric and statistical software.

Key contract research projects include an analysis of the macroeconomic impacts of local content legislation and an analysis of the economy-wide effects of the FCC access charge plan. Major model development projects include a redesign of Wharton's multiregion model of New York State and respecification and updating of Wharton's Quarterly Model.

Vice President, U.S. Modeling Services — 1/80-6/83

Responsible for coordinating model development/enhancement activities of Wharton's U.S. forecasting services, including the Long-Term Forecasting Model, the Quarterly Forecasting Model, and Industry Planning Service Model.

Worked with the marketing group and the model project directors to develop new sources of revenue for the U.S. model-based forecasting services from both subscription and contract research sources.

Executive Director, Wharton Annual (Long-Term) Model Project 1/77-12/79

Responsible for directing model development/enhancement, forecasting, scenario analysis, contract research, forecast review meetings, and client support activities for U.S. Long-Term Forecasting Service.

Under the direction of Dr. Schink, the Wharton Annual Model was expanded in scope (from 850 variables to 2300 variables) to incorporate energy detail, demographic detail, and producer price detail. These changes were designed to enhance the Annual Model's usefulness for long-term planning and analysis. Research and development contracts to support the Long-Term Model enhancement activities were obtained from the Federal Energy Administration, the Electric Power Research Institute, the Office of Naval Research, Ross Laboratories, and the U.S. Department of Energy.

These model enhancement activities have led to contracts to perform long-term policy and scenario analyses for the groups supporting development as well as contracts from others such as the American Gas Association, the Whirlpool Corporation, the New York Stock Exchange, the General Accounting Office, the Joint Economic Committee, the U.S. Department of Commerce, Sun Oil Company, and the U.S. Department of Defense.

Executive Director, Special Projects 6/72-1/77

Directed the Commodity Model Maintenance Project (a joint effort with Charles River Associates, Inc.). This project involved the development of econometric models of the world markets for nonferrous mineral commodities. These models were used to produce five-year projections of demand, supply, and price, and to evaluate the effects of alternative General Services Administration commodity disposal patterns on these commodity markets. Over a four-year period, twelve markets were analyzed: Cobalt, Copper, Chromite, Lead, Manganese, Mercury, Molybdenum, Platinum-Palladium, Rubber, Tin, Tungsten, and Zinc.

Developed a regional econometric model of Luzerne County, Pennsylvania, to evaluate the effects of Hurricane Agnes on this area.

Developed a large model of the U.S. auto industry based on time-series and cross-section data. This model, which was developed for the Transportation Systems Center of the U.S. Department of Transportation, was designed as a tool to investigate the longer-term determinants of the size and composition of the U.S. auto fleet and to provide a tool for the analysis of various potential policy initiatives.

Developed a model based on cross-section data for the National Association of Broadcasters to analyze the effects of increasing the number of imported signals carried via cable systems on the audience for local stations.

Participated in the development of Wharton's timesharing software system. Dr. Schink was involved in the selection of a time-sharing vendor, assembly of the programming staff, specification of the software capabilities, the incorporation of Wharton data bases and models in the new software system, the development of documentation and the initial marketing effort.

Participated in the design of the Wharton World Model system.

UNIVERSITY OF PENNSYLVANIA, Philadelphia, PA — Spring '73
Visiting Lecturer

THE BROOKINGS INSTITUTION, Washington, D.C.

Principal Investigator, Quarterly Model Project — 6/69-6/72

Responsible for directing the staff of the model project with guidance from senior advisors (primarily Lawrence R. Klein and Gary Fromm).

Specified and estimated the version of the Brookings Model which was used to perform

EDUCATION

Ph.D. in Economics, University of Pennsylvania, 1971

Thesis (Unpublished): Small Sample Estimates of the Variance Covariance Matrix of Forecast Error for Large Econometric Models: The Stochastic Simulation Technique. Won William Carey Prize for best Ph.D. thesis in economics at the University of Pennsylvania, 1971. Thesis Advisor: Professor Lawrence R. Klein

B.S. in Economics, University of Wisconsin at Madison, 1964

PROFESSIONAL HONORS AND ASSOCIATIONS

Board of Directors, Wharton Econometric Forecasting Associates, 1972-87.
William Carey Prize for Best Thesis in Economics, U of PA.
Ford Foundation Dissertation Grant, 1967.
Research Fellowship, Economic Research Unit, University of PA.
Member, American Economic Association & the Econometric Society.

PUBLISHED ARTICLES

"Short and Long Term Simulations with the Brookings Model" (with Gary Fromm and Lawrence R. Klein), in Bert G. Hickman (ed.) Econometric Models of Cyclical Behavior, New York: Bureau of Economic Research, 1972.

"Aggregation and Econometric Models" (with Gary Fromm), International Economic Review, February 1973.

"A Disaggregated Quarterly Model of U.S. Trade and Capital Flows: Simulations and Tests of Policy Effectiveness" (with Sung Y. Kwack), in Gary Fromm and Lawrence R. Klein (eds.), The Brookings Model: Perspective and Recent Developments, Amsterdam and New York: North-Holland Publishing Co. and American Elsevier Publishing Co., Inc., 1975.

"An Evaluation of the Predictive Abilities of a Large Model: Post-Sample Simulations With the Brookings Model," in Gary Fromm and Lawrence R. Klein (eds.), The Brookings Model: Perspective and Recent Developments, Amsterdam and New York: North-Holland Publishing Company and American Elsevier Publishing Company, Inc., 1975.

"The Brookings Quarterly Model: As An Aid to Longer Term Economic Policy Analysis," International Economic Review, February 1975. Reprinted in Lawrence R. Klein and Edwin Burmeister (eds.) Econometric Model Performance: Comparative Simulation Studies of the U.S. Economy, Philadelphia: University of Pennsylvania Press, 1976.

"An Overview of Econometric Model Building In And Of the U.S.A.: Subnational Macro Econometric Modeling," published in Proceedings of the NSF-CNRS Conference on Macroeconometric Models and Economic Forecasting, Universite de Paris, X-Naterre, November 22-26, 1976.

"The International Tin Agreement: A Reassessment" (with Gordon W. Smith), Economic Journal, December 1976, Reprinted in United Malaysia Bank Corporation Economic Review, Vol. 13, No.2, 1977.

"The Practice of Macroeconometric Model Building and Its Rationale." (with E.P. Howrey, L.R.

Analysis of the Macroeconomic Impacts of the Proposed NHTSA Passenger Car MPG Standards, prepared for the Chase Manhattan Bank, N.A., 1 Chase Manhattan Plaza, New York, N.Y. 10015, January 1979.

[redacted]